

## TITLE 10. CALIFORNIA DEPARTMENT OF FINANCIAL INSTITUTIONS FINDING OF EMERGENCY

Pursuant to Government Code Section 11346.1, the California Commissioner of Financial Institutions ("Commissioner") hereby amends Title 10, Chapter 1, of the California Code of Regulations by adopting Subchapter 4, entitled, "The California Foreclosure Prevention Act." These emergency regulations clarify the application of Sections 2923.52 and 2923.53 of the Civil Code under the California Foreclosure Prevention Act ("CFPA", Civil Code Sec. 2923.52 et seq.), as enacted by ABX2 7 (Lieu, Ch. 5, Stats. 2009) and ABX2 7 (Corbett, Ch. 4, Stats. 2009) during the second extraordinary legislative session.

### INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

On February 20, 2009, Governor Schwarzenegger signed into law the CFPA to assist in slowing the ongoing foreclosure crisis in California. The CFPA provides specified borrowers an additional 90 days in the home foreclosure process, unless the mortgage loan servicer responsible for servicing the borrower's loan establishes that it has implemented a comprehensive loan modification program, as described in Civil Code Section 2523.53, and the servicer obtains an order, as specified, from the Commissioner of Corporations, Financial Institutions, or Real Estate. The order from the Commissioner of Corporations, Financial Institutions, or Real Estate exempts a mortgage loan servicer from the requirement in Civil Code Section 2523.52(a) that a borrower be provided an additional 90 days in the home foreclosure process. The purpose of the CFPA is to encourage mortgage loan servicers to implement comprehensive loan modification programs to assist homeowners in paying their mortgage obligations and retaining their homes.

Civil Code Section 2523.53(d) requires the Commissioners of Corporations, Financial Institutions, and Real Estate to adopt emergency regulations to clarify the application of Civil Code Sections 2523.52 and 2523.53. Accordingly, these rules clarify these sections as follows.

### CFPA

The CFPA requires a trustee to provide certain borrowers an additional 90 days in the foreclosure process, as specified, unless the residential mortgage servicer has obtained an order from the Commissioner of Corporations, Financial Institutions, or Real Estate exempting it from this requirement. A servicer may obtain an order by establishing and implementing a comprehensive loan modification program, as set forth in the CFPA, and submitting an application to appropriate Commissioner documenting the program.

These emergency regulations set forth the requirements for a comprehensive loan modification program, the process to apply for an order of exemption, the application for an order of exemption, and the reporting of data.

### Federal Home Affordable Modification Program

The regulations provide that a loan modification program in compliance with the federal Home Affordable Modification Program ("HAMP") constitutes a comprehensive loan modification program under the CFPA. On March 4, 2009, the Obama Administration released U.S. Department of the Treasury guidelines to allow servicers to begin immediately modifying eligible loans under the HAMP, a program designed to

encourage loan modifications, similar to CFPB. The guidelines define a waterfall process of modifying a home loan in order to achieve a debt to income ratio of 31% by first lowering the interest rate to as low as 2%, next extending the term of the loan to as much as 40 years, and finally forbearing principal on the loan until the maturity date of the loan. The features of the federal program are at least as inclusive as the features of the CFPB, and therefore these rules provide that compliance with HAMP meets the requirement for enacting a comprehensive loan modification program. Because this federal program requires participating servicers to modify the loans of all eligible borrowers, a servicer would not need any additional state program to obtain an order of exemption from the appropriate Commissioner and the rules provide that no other requirements are applicable to servicers who have implemented HAMP.

#### Other Federal Programs

The rules provide that loans refinanced or modified under other federal programs, such as the Hope for Homeowners program or the Home Affordable Refinance Program, meet the requirements of the state comprehensive loan modification program for those particular loans. If a servicer has additional borrowers and loans that meet the eligibility requirements for the state program, the servicer must have implemented a program consistent with the state requirements for the remaining loans, to obtain the order of exemption.

#### Eligibility

The rules require a comprehensive loan modification program to be made available to all borrowers and loans meeting specified minimum requirements. A servicer may have a broader program, but not have a more restrictive program, to obtain the order of exemption.

The minimum eligibility requirements include the following:

- The borrower requesting the modification occupies the property, is in default on the loan, is not in a bankruptcy proceeding, can document income, and has not surrendered the property.
- The loan was made from 2003 through 2007, is the first lien on the property, and is secured by property in California.

#### Availability

The rules require servicers to alert borrowers to the existence of the program during the contact required under last year's SB 1137 (Perata, Ch. 69, Stats. 2008), which among other things requires a lender to reach out to a borrower at least 30 days before filing a notice of default on a property. Servicers are required to allow participation in the servicer's comprehensive loan modification program for any eligible borrower who contacts the servicer requesting assistance.

#### Minimum Program Requirements

The rules set forth minimum program requirements that generally reflect and clarify the requirements of the CFPB.

##### a. Anticipated Recovery (NPV) Test

The rules provide that a servicer may use the NPV parameters in the HAMP. If a

servicer does not use these parameters, the servicer must specify the parameters and assumptions in its NPV test, and explain in its application why the assumptions are reasonable. A servicer must offer a loan modification to any borrower where the NPV of modifying the loan is greater than the NPV of foreclosure.

b. Debt to Income Ratio

The rules provide that a servicer's program must seek to achieve an aggregate 38% debt-to-income ratio. For loans not modified at or below 38%, a servicer must explain in its application the borrower characteristics that result in a higher ratio modification.

c. Other Features

The rules set forth additional features for a modification program as set forth in the CFPA: interest rate reductions, reduction in principal, extension of the amortization period, and other factors set forth in the application and approved by the Commissioner. Consistent with the statute, the rules require that a plan include at least two of the features, but clarifies that a loan modification does not need to include more than a single feature.

d. Sustainability

The CFPA requires that a servicer seek to achieve long term sustainability for a borrower. The rules include a list of characteristics that demonstrate long-term sustainability, including a reduction in monthly payment, a 38% or lower debt to income ratio, a back-end debt to income ratio of less than 55%, and a current loan 3 months after modification.

e. Other Requirements

The rules include other requirements intended to further delineate the necessary requirements for a comprehensive loan modification program, including the following:

- That a repayment plan, without more, will not constitute a loan modification unless the borrower achieves a 38% or less debt to income ratio, and the servicer has verified the borrower's ability to repay the loan;
- That the servicer must make a reasonable effort to obtain the consent of the subordinate lien holder to subordinate the lien to the modified loan, where necessary for the servicer to proceed with a modification;
- That a servicer must make a reasonable effort to obtain the consent of investors to a modification, and must have reasonable grounds for concluding that a pooling-servicing agreement prevents a modification; and
- That procedures be implemented to permit a servicer to act on applications timely, and not prejudice a borrower by delay.

Application

The rules set forth instructions on filing an application, receiving a temporary order, and receiving a final order of exemption. The rules further include the application.

### Data

In accordance with the CFPA, the rules set forth loan modification data to be submitted to the appropriate Commissioner on a quarterly basis. The data to be collected includes information on the volume of foreclosures, modifications, modifications by type, and redefaults, and information on the reasons for denying modifications. The rules further permit the Commissioners to grant hardship exemptions, as specified.

### Public Participation

On April 21, 2009, the Departments of Corporations, Financial Institutions and Real Estate released a draft of the rules, application, and reporting requirements to interested parties in accordance with Government Code Sections 11346(b) and 11346.45. The comments from interested parties were evaluated, and changes were made to the draft rules to incorporate changes, where appropriate.

### Timing

The CFPA was enacted as part of the second extraordinary legislation session, was signed on February 20, 2009, and becomes effective May 21, 2009 (91 days after the session is adjourned, or 91 days after February 19, 2009). The CFPA requires emergency regulations to be adopted 10 days after the effective date of the CFPA, and provides that the act is operative 14 days after this issuance of regulations. As a result, the Department of Financial Institutions (the "Department") is requesting the emergency regulations to be filed with the Secretary of State on June 1, 2009 (see Government Code Section 6800), thereby making the law operative on June 15, 2009. This request is intended to provide certainty to the marketplace about the operative date of the CFPA.

### AUTHORITY

Sections 2923.52 and 2923.53, Civil Code.

### REFERENCE

Sections 2923.52 and 2923.53, Civil Code.

### FINDING OF EMERGENCY

The Commissioner hereby finds that these emergency regulations are necessary for the immediate preservation of the public peace, health and safety, or general welfare for the reasons set forth in Section 2 of ABX2 7 and SBX2 7:

*(a) California is facing an unprecedented threat to its state and local economies due to skyrocketing residential property foreclosure rates in California. Those high foreclosure rates have adversely affected property values in California, and will have even greater adverse consequences as foreclosure rates continue to rise.*

*(b) It is essential to the economic health of California for the state to ameliorate the deleterious effects that will result from the continued high rate of foreclosure of residential properties by modifying the foreclosure process to provide additional time for borrowers to work out loan modifications while providing an exemption for mortgage loan servicers that have implemented a comprehensive loan modification program. This change in accessing the state's foreclosure process is essential to ensure that the process does not exacerbate the current*

*crisis by adding more foreclosures to the glut of foreclosed properties already on the market if the foreclosure may be avoided through a loan modification. Those additional foreclosures could further destabilize the housing market with significant, corresponding deleterious effects on the state and local economies.*

The Department does not have sufficient time to enact a regulation through the rulemaking process in order to have the rule in place upon the operative date of ABX2 7 and SBX2 7. Further, Section 2923.53(d) of the CFPB directs the Commissioner to adopt emergency rules to clarify the act. Consequently, the Commissioner is adopting these emergency regulations. This finding of emergency is supported by the case of Schenley Affiliated Brands Corp. v. Kirby, 21 Cal. App. 3d 177 (1971), where the court deferred to the agency's determination that an impending deadline constituted an emergency under the Administrative Procedure Act.

#### LOCAL MANDATE

These regulations do not impose a mandate on local agencies or school districts.


#### COST OR SAVINGS TO STATE AGENCY

These regulations will not result in any cost or savings to any local agency or school district, nor any other nondiscretionary cost or savings on local agencies. These regulations will not result in any cost or savings in federal funding to the state. These regulations will not result in any cost or savings to any state agency; any costs on a state agency are attributable to the statutes mandating these regulations.

#### CONTACT PERSON

Inquiries concerning this action may be directed to Kenneth Sayre-Peterson, Acting General Counsel, Department of Financial Institutions, at (916) 322-1570. The backup contact person is Paul Crayton at (415) 263-8541. Written inquiries may be submitted to the Department of Financial Institutions, Legal Division, 1810 – 13<sup>th</sup> Street, Sacramento, California, 95811.

Dated: May 14, 2009  
Sacramento, California

  
KENNETH SAYRE-PETERSON  
Acting General Counsel